STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition of AMHERST CABLEVISION, INC. for Redetermination of a Deficiency or for Refund of Corporation Tax under Article 9 of the Tax Law for the Year 1985.	:	
In the Matter of the Petition of KEN-TON CABLEVISION, INC. for Redetermination of a Deficiency or for Refund of Corporation Tax under Article 9 of the Tax Law for the Year 1985.	:	DETERMINATION DTA NOS. 806105, 806106, 806107, 806808 AND 806809
In the Matter of the Petition of AMHERST CABLEVISION, INC. for Redetermination of a Deficiency or for Refund of Corporation Tax under Article 9 of the Tax Law for the Year 1986.	:	
In the Matter of the Petition of KEN-TON CABLEVISION, INC. for Redetermination of a Deficiency or for Refund of Corporation Tax under Article 9 of the Tax Law for the Year 1986.	:	

In the Matter of the Petition

of

COMAX TELECOM CORPORATION

for Redetermination of a Deficiency or for Refund of Corporation Tax under Article 9 of the Tax Law for the Year 1986.

Petitioners Amherst Cablevision, Inc. and Ken-Ton Cablevision, Inc., 3000 One American Center, Austin, Texas 78701, filed petitions for redetermination of deficiencies or for refund of corporation tax under Article 9 of the Tax Law for the year 1985.

Petitioners Amherst Cablevision, Inc., Ken-Ton Cablevision, Inc. and Comax Telecom Corporation, 3000 One American Center, Austin Texas 78701, filed petitions for redetermination of deficiencies or for refund of corporation tax under Article 9 of the Tax Law for the year 1986.

A consolidated hearing was commenced on September 12, 1990 before Timothy J. Alston, Administrative Law Judge, and continued before Jean Corigliano, Administrative Law Judge, on March 10, 1993 and continued to completion on May 26, 1993.[1] Petitioners' final

[1]The petitions of Amherst Cablevision, Inc. and Ken-Ton Cablevision, Inc. for the year 1985 (DTA Nos. 806808 and 806809) were not a subject of the hearing commenced before Judge Alston, but were later consolidated with the matters before him -- the petitions of Amherst Cablevision, Inc., Ken-Ton Cablevision, Inc. and Comax Telecom Corporation for the year 1986.

brief was filed on June 1, 1994 which began the statutory period for issuance of a determination. Petitioners appeared before Judge Alston by Moot & Sprague (Arnold N. Zelman, Esq., of counsel). Petitioners appeared before Judge Corigliano by Whitman, Breed, Abbott & Morgan (Brian E. Gledhill, Esq., and Michael S. Press, Esq., of counsel). The Division of Taxation appeared by William F. Collins, Esq. (Deborah J. Dwyer, Esq., and Robert Tompkins, Esq., of counsel).

ISSUE

Whether the Division of Taxation may assert tax deficiencies against petitioners under Article 9 of the Tax Law.

FINDINGS OF FACT

These matters have a rather complex procedural history. Before detailing that history, it will be helpful to begin with a brief summary. Each of the petitioners, Amherst Cablevision, Inc. ("Amherst"), Ken-Ton Cablevision, Inc. ("Ken-Ton") and Comax Telecom Corporation ("Comax") were issued notices of deficiency under Article 9 of the Tax Law. After those notices were issued, the Tax Appeals Tribunal issued a decision in an unrelated case holding that a provider of cable television programming, was not subject to the tax on transmission companies imposed by Article 9 of the Tax Law, but rather was a general business corporation subject to tax under Article 9-A of the Tax Law (Matter of Capital Cablevision Systems, Tax Appeals Tribunal, June 9, 1988). Based on this decision, the Division of Taxation ("Division") took the position that petitioners were liable for the tax imposed by Article 9-A of the Tax Law and issued notices of deficiency to petitioners under Article 9-A. Some procedural skirmishing followed. A hearing was held and completed on May 26, 1993 where the only issue addressed was whether in the years 1985 and 1986 petitioners were subject to the tax imposed by Article 9-A of the Tax Law. Petitioners filed a brief on August 30, 1993, addressing that issue. In September 1993, the Tax Appeals Tribunal issued a decision where it held that cable companies

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On April 25, 1991, Judge Alston issued an interim order regarding those petitions which were before him.

were entitled to rely on the Division's long-standing policy requiring them to file under Article 9 of the Tax Law and that any change in that policy could not be applied retroactively by the Division (Matter of Newchannels Corp., Tax Appeals Tribunal, September 23, 1993). The Division then requested and received an extension of time in which to file a brief. By letter dated December 9, 1993, the Division expressed its view that the issue had shifted back to whether petitioners were liable for tax under Article 9 of the Tax Law. Briefs were exchanged by the parties addressing this issue. With this background, the history of this case will now be detailed.

The 1985 Deficiencies

On October 30, 1987, the Division issued notices of deficiency to Amherst and Ken-Ton, asserting tax deficiencies against each under Article 9 of the Tax Law for the calendar year 1985. Notice number C870914461N issued to Amherst asserted a tax due of $939.06 and notice number C870914460N issued to Ken-Ton asserted a tax due of $1,010.38. Amherst and Ken-Ton each made a timely request for a conciliation conference to challenge the notices.

On or about September 16, 1988, the Division sent Amherst and Ken-Ton similar letters, purportedly revising the tax asserted by the notices of deficiency to reflect tax due under Article 9-A of the Tax Law. Each letter included the following statement:

> "As indicated above, the assertion of a greater deficiency is done in accordance with Section 1089(d)(1) of the Tax Law which states in part, 'The Tax Commission shall have the power to determine a greater deficiency . . . if claim therefor is asserted at or before the hearing . . . .'"

The Division later issued statements of audit adjustment to Amherst and Ken-Ton, dated November 18, 1988. Each statement contains this explanation:

> "Based on the decision reached In the Matter of the Petition of Capitol [sic] Cablevision Systems, Inc. it was determined that corporations engaged in cable television are taxable under Article 9A, not Article 9 of the Tax Law. The above assessment is based on this decision."

The Statement of Audit Adjustment issued to Amherst (Assessment number C881118460N) contains this calculation of tax due under Article 9-A:

"Net income		$1,314,857.00
New York State allocation	100%	

Allocated income		1,314,857.00
Taxable at 10%		131,485.70
Tax paid under Sections 183 and 184		49,293.19
Deficiency		82,192.51"

The Statement of Audit Adjustment issued to Ken-Ton (Assessment number C881118462N) contains this calculation of tax due under Article 9-A:

"Net income		$1,485,166.00
New York State allocation	100%	
Allocated New York income		1,485,166.00
Taxable at 10%		148,517.00
Tax paid under Sections 183 and 184		44,684.67
Deficiency		103,832.33"

On January 4, 1989, the Division issued notices of deficiency to Amherst and Ken-Ton under Article 9-A. The notice issued to each petitioner shows the same amount of tax due as asserted in the corresponding Statement of Audit Adjustment and bears the same assessment number as that appearing on the statement.

On or about January 20, 1989, the Division issued conciliation orders to Amherst and Ken-Ton. Each Conciliation Order shows the "Tax Article No." as "9A". The Conciliation Order issued to Amherst shows the Notice Number as C870914461N, which corresponds to the number on the original notice issued under Article 9, and sustains that notice. The Conciliation Order issued to Ken-Ton sustains notice number C870914460N which is the number on the notice issued to Ken-Ton under Article 9.

On February 1, 1989, the Division issued individual notices to Amherst and Ken-Ton. Each notice states: "As a result of your correspondence and/or recent conference, the balance of the above assessment has been cancelled" (original in capital letters). In each case, the assessment number shown on the notice corresponds to the number appearing on the Notice of Deficiency issued on January 4, 1989, asserting tax due under article 9-A of the Tax Law. In short, as of February 1, 1989 the only extant 1985 assessments against Amherst and Ken-Ton were the original notices issued on October 30, 1987 under Article 9 of the Tax Law.

On April 17, 1989, the Division of Tax Appeals received the petitions of Amherst and Ken-Ton. By those petitions, Amherst and Ken-Ton challenged taxes assessed under both

Article 9 and Article 9-A of the Tax Law.[2] Amherst and Ken-Ton alleged that the Commissioner of Taxation and Finance erred in applying the holding of Capital Cablevision Systems retroactively and recalculating tax due under Article 9-A of the Tax Law. The petitions indicate that Amherst and Ken-Ton conceded the Division's authority to revise the outstanding notices of deficiency issued under Article 9 by recalculating the tax under Article 9-A in accordance with the Division's letter of September 16, 1988.

In its answer to the petitions of Amherst and Ken-Ton, the Division denied each of petitioner's allegations of error and affirmatively asserted:

> "that the Audit Division revised certain deficiencies issued against the Petitioners' [sic] based on the New York State Tax Appeals Tribunal Decision In the Matter of the Petition of Capital Cablevision Systems, Inc., STATES that said decision determined that corporations engaged in cable television are taxable under Article 9A of the Tax Law."

The 1986 Deficiencies

On July 7, 1988, the Division issued statements of audit adjustment to Amherst, Ken-Ton and Comax, asserting deficiencies in tax under Article 9, section 184, of the Tax Law for the calendar year 1986. In each case, the Statement of Audit Adjustment indicated that the tax was imposed on gains from the sale of intangibles. The total tax asserted against Amherst was $163,264.00; the total tax asserted against Ken-Ton was $131,040.00; and the total amount asserted against Comax was $346,557.00. On August 29, 1988, the Division issued notices of deficiency to petitioners asserting the same tax deficiencies as shown on the statements of audit adjustment.

On October 4, 1988, petitioners filed petitions with the Division of Tax Appeals challenging the notices issued under Article 9. In each petition, the petitioner alleged that the Commissioner erred by determining that the gain on the sale of intangible assets is subject to tax under Article 9 of the Tax Law. Each petitioner alleged that all of its assets were sold

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[2]Whether petitioners simply understood that the Division did not intend to cancel the Article 9-A deficiencies or some other communication passed between the parties is not known.

pursuant to a contract which allocated the purchase price between tangible and intangible assets. Each petitioner claimed that "gross earnings" as that term is used in Article 9 does not include gain from the sale of intangible assets.

On November 18, 1988, the Division issued statements of audit adjustment to Amherst and Ken-Ton (but not to Comax) asserting tax due under Article 9-A of the Tax Law. The amount of tax asserted against Amherst was $1,113,225.80, and the amount of tax asserted against Ken-Ton was $937,139.57.

Pursuant to State Administrative Procedure Act § 306(4), official notice is taken of the fact that the Division filed an answer to the petition of Comax on or about January 10, 1989. A copy of that answer was filed with the Division of Tax Appeals, although it was not placed in evidence by the parties. The answer denied all of the allegations contained in paragraphs (3), (4), (5) and (6) of section II of the petition; asserted that under section 184 of Article 9 of the Tax Law gross earnings includes earnings from the sale of intangible assets; and alleged that a penalty was properly imposed because petitioner failed to supply information to the Division. The Division requested that the Notice of Deficiency issued to Comax on August 29, 1988 in the amount of $346,557.00 be sustained. On January 19, 1989 the Division filed an amended answer to Comax's petition, expanding its denials to include paragraphs (7) through (12) of section II of the petition. The Division's answer and amended answer made no mention of Article 9-A of the Tax Law.

On January 19, 1989, the Division filed its answer to the petition of Amherst. The answer denied all of petitioner's allegations; asserted that under section 184 of Article 9 of the Tax Law gross earnings includes earnings from the sale of intangible assets; and alleged that a penalty was properly imposed because petitioner failed to supply information to the Division. The answer was silent concerning the Statement of Audit Adjustment issued two months earlier asserting tax under Article 9-A.

On February 1, 1989, the Division issued notices to Amherst and Ken-Ton cancelling the notices of deficiency issued to each under Article 9 of the Tax Law. This explanation is

given for the cancellation: "As a result of your correspondence and/or recent conference the balance of the above assessment has been cancelled" (original in capital letters). The Statement of Audit Adjustment issued to Ken-Ton on July 7, 1988 bears the following handwritten notation: "TC34 to cancel L Martinez dup assmt corp is taxable as 9A."

On February 8, 1989, the Division filed an answer to the petition of Ken-Ton, denying petitioner's allegations. It contains the same affirmative allegations with regard to petitioner's liability under section 184, Article 9, of the Tax Law as are contained in the answers to the petitions of Comax and Amherst. The answer is silent about the cancellation of the Article 9 notice on February 1, 1989 and the issuance of the statement of audit adjustment under Article 9-A of the Tax Law in November 1988.

On September 27, 1989, the Division issued notices of deficiency under Article 9-A of the Tax Law to Amherst and Ken-Ton, asserting tax deficiencies in the same amounts as those asserted in the November 1988 statements of audit adjustment.

By letter to the Division's attorney, Deborah J. Dwyer, dated November 15, 1989, petitioners' attorney, Arnold Zelman, outlined petitioners' position with regard to the pending petitions. The letter states, in relevant part:

> "I am writing to make sure there is no misunderstanding as to the position of the above named Taxpayers in the hearings presently pending before the Division of Tax Appeals . . . .
>
> "Initially, the State of New York assessed deficiencies against the Taxpayers on the grounds that the returns filed by them under Article 9 of the Tax Law contained errors . . . . Taxpayers duly filed their petition with the Division of Tax Appeals and the State duly answered. Issue was joined and hearing was set for early December.
>
> "Subsequently, when Taxpayers requested that you agree to certain stipulations, you informed Taxpayers that the State will not be trying the issue because of its cancellation of the Article 9 Notices of Deficiency . . . .
>
> "As we see it, if the State is really considering changing its theory of liability and the amount owed for the years now before the Division of Tax Appeals, it can do so - if at all - only by moving to amend the pleadings it has filed in the cases currently pending. While Taxpayers have not researched whether the State can now amend its theory of liability - and preserve any claims they may have to request a denial of the State's motion to amend or to quash such amended pleadings - Taxpayers will assert at the least that, under the rules of procedure governing Division of Tax Appeals proceedings, the State will have the burden of

proof with regard to the changed theory and the asserted increased tax liability, if any. In addition, once the State's pleadings are so amended, Taxpayers will seek a continuance on the basis of surprise.

"Taxpayers believe that the State cannot 'start over' with impunity and just ignore the legal processes which have already transpired or the current posture of the cases. It may very well be too late for the State to decide it assessed deficiencies under the wrong statute (and Taxpayers vigorously deny any liability under either Article 9 or Article 9-A). At the least, however, as stated above, if the State wishes to change its theory or the amount of the deficiency, it must seek to amend its pleadings and assume the burden of proof with respect to same. Taxpayers would vigorously contest any motion to amend which fails to incorporate Taxpayers [sic] position as described herein."

A letter from Mr. Zelman to Ms. Dwyer, dated November 28, 1989, states:

"This will confirm our recent telephone conversation wherein you advised me that the State will promptly move to amend its Answers in the above-referenced cases so as to allege an increased tax deficiency by reason of changing the theory of taxation from Article 9 to Article 9-A of the Tax Law. You also agree that the State will have the burden of proof in these cases by reason of such amendment. I assume that the State will cancel Notices of Deficiency which it had issued on September 27, 1987 [sic] for Amherst Cablevision, Inc. and Ken-Ton Cablevision, Inc.

"However, Petitioners cannot agree that the State is entitled to amend its Answers to conform them to the evidence. Section 3000.4(c) provides that such a motion can be made before the Hearing is concluded and, as you know, the Hearing has not yet begun. We believe you must move to amend and serve amended Answers before the Hearing has commenced. As a matter of fact, Petitioners will be prejudiced if this is not done in such manner."

On December 29, 1989, the Division sent similar letters to Amherst, Ken-Ton and Comax. The letters sent to Amherst and Ken-Ton state that the purpose of the letter is (1) to formally assert an additional franchise tax deficiency for 1986 "in supplement to" the notice issued on July 7, 1988 under Article 9 and (2) to clarify the Division's position regarding the status of the administrative proceeding commenced by petition of the Article 9 notices. In each letter, the Division asserted that its purpose in issuing notices of deficiency under Article 9-A was "merely to assert an additional franchise tax deficiency for 1986." Each letter states:

"[T]he cancellation notice issued in regard to [the notice of deficiency issued on July 7, 1988] should be deemed a nullity. It should be noted that your client did not sign off on this cancellation notice; therefore, the administrative proceeding pertaining to this notice was never concluded.

"In summary, [the notice of deficiency issued on September 27, 1989] need not be petitioned because it is, in effect, a de facto notice of claim asserting an additional deficiency. The original notice remains intact, and additional deficiency

is asserted in an amount listed below."

Each letter then provided a computation of tax due for 1986 under Article 9-A of the Tax Law. Penalty was cancelled.

Since the Division had never cancelled the original Article 9 assessment issued to Comax, it was not necessary for it to clarify its position regarding that notice. The letter sent to Comax merely states that the original notice was revised to reflect tax under Article 9-A of the Tax Law, and it shows a recalculation of the tax deficiency under Article 9-A.

After receiving the letters of December 29, 1989, Mr. Zelman repeated his earlier assertions (1) that the Division was required to amend its answer if it was going to assert additional deficiencies under Article 9-A of the Tax Law, (2) that it could not amend without seeking permission to do so from the Tax Appeals Tribunal, (3) that petitioners were not required to petition the Division's letters of December 29, 1989, and (4) that the Division had the burden of proof with regard to the Article 9-A deficiencies. In a letter to the Supervising Administrative Law Judge, dated January 29, 1990, the Division's attorney stated that the Division did not believe that it had an obligation to file an amended answer and that petitioners should, instead, file amended petitions. To resolve the dispute between the parties, a hearing was scheduled before Administrative Law Judge Timothy J. Alston.

At the hearing before Judge Alston, the primary issue discussed was whether the Division followed the proper procedure when it issued the letters of December 29, 1989 asserting tax deficiencies under Article 9-A. The Division's position, as stated by its representative at that hearing, was (1) that the Division could no longer pursue a claim for taxes under Article 9 and (2) that the December 29th letters acted as notices of claim for additional taxes due under Tax Law § 1089(d)(1). If the notices were not deemed to satisfy the requirements of section 1089(d)(1), the parties asked Judge Alston to determine what form the assertion of the Article 9-A deficiencies should take.

Petitioners argued that the only way in which the Division could assert additional deficiencies was by filing amended answers. They took the position that no evidence could be

submitted regarding the Article 9-A taxes until amended pleadings were filed putting those taxes in issue.

The Division objected to filing an amended answer on the ground that it would be procedurally confusing. The Division's attorney also stated that the letters of December 29, 1989 provided the petitioners with adequate notice of the Division's position and that the filing of an amended answer would simply be redundant. In an attempt to clarify the Division's position, Judge Alston stated to Ms. Dwyer:

> "But you do take the position, do you not, that by your -- by the issuance of the December 29th letter, you do take the position that that notice dated 8/29/88 was canceled, in effect canceled and you're changing your theory of liability -- I mean, wait, excuse me. You take the position that the Notice is still good, but you're asserting liability under the other article, correct?"

Ms. Dwyer responded: "That's correct." (Tr., pp. 32-33.)

Judge Alston issued a determination on April 25, 1991 where he ordered the Division to file amended answers and ordered petitioners to file replies to those answers. The Division then filed a consolidated amended answer to the petitions of Amherst, Ken-Ton and Comax where it alleged as follows:

> "1. AFFIRMATIVELY STATES that the Tax Appeals Tribunal issued a decision, Matter of Capital Cablevision Systems, Inc. on June 9, 1988.
>
> "2. AFFIRMATIVELY STATES that as a result of the decision cable television companies, which were previously improperly taxed under Article 9, were deemed to be properly taxable under Article 9A.
>
> "3. AFFIRMATIVELY STATES that the Petitioner corporations are cable television companies and therefore within the purview of Matter of Capital Cablevision.
>
> "4. AFFIRMATIVELY STATES that as a result of the decision the Audit Division supplemented its original notice with a notice of claim for additional taxes due on December 29, 1989; said notices outlined the basis for the additional tax due under Article 9A and included a computation of tax due for each corporation. (Notices of claim attached hereto).
>
> "5. AFFIRMATIVELY STATES that based on the foregoing, the Audit Division asserts that by the decision rendered by the Tribunal in Capital Cablevision, the Petitioner corporations are properly taxable under Tax Article 9A.
>
> "6. AFFIRMATIVELY STATES that pursuant to Section 1089(e)(3) the Audit Division has the burden of proof with respect to the additional tax asserted by its notices of claim; accordingly the Audit Division need only show that it

properly assessed Article 9A tax pursuant to Section 208.9 based on 'entire net income'.

"7. AFFIRMATIVELY STATES that the Petitioner has the burden of proof to establish that the Assessment is erroneous and/or improper."

Petitioners filed a reply to the amended answer denying that they are subject to tax under Article 9-A, affirmatively alleging that they are subject to tax under Article 9 and alleging that "the returns filed by Petitioners under Article 9 were correct as filed."

The 1985 and 1986 Deficiencies

The administrative hearing was continued on March 10, 1993. The Division's attorney made the following opening statement:

"Briefly, to state the issue before you, was the Audit Division correct when it made the determination pursuant to Capital Cablevision, decided by the Tribunal on June 9th, 1988, that the Petitioners herein should be taxed under Article 9-A rather than Article 9.

"Prior to Capital Cablevision, the Petitioner had been taxed under Article 9. Once the decision was rendered in Capital Cablevision, the Audit Division believed it was bound by the terms of that decision and, accordingly, changed the long-standing policy that cable companies were taxable under Article 9 and instead, taxed all cable companies under Article 9-A.

"The Petitioner has objected to the change on several grounds, stating that--of course, he will elaborate on this--Capital Cablevision does not apply to their particular business and that Capital was improperly retroactively applied.

"It would be for you to determine whether or not the Audit Division acted properly in this matter." (Tr., p. 66.)

Later in the proceeding, the following exchange took place between the Administrative Law Judge and the Division's attorney:

Q: "Thank you. This is probably covered in your Stipulations but let me ask to clarify in my own mind. The notices of deficiency [issued] under Article 9, Miss Dwyer, were those withdrawn or are you asserting a new deficiency--"

A: "They were, in essence, cancelled and new deficiencies issued under Article 9-A."

Q: "Meaning the letters issued in December 1989."

A: "Yes." (Tr., p. 77.)

The parties executed and submitted into evidence seven stipulations and numerous exhibits. The First Stipulation contains the following statement:

"As of the date of this stipulation, the Department does not assert any Tax Law Article 9 deficiency against Amherst, Comax or Ken-Ton for calendar years 1985 or 1986."

The First Stipulation is dated November 1991 and signed by Deborah J. Dwyer for the Division. Among the exhibits stipulated into evidence were the Article 9 franchise tax reports filed by petitioners for the years in issue and petitioners' 1985 and 1986 Federal income tax returns.

Based on the Federal income tax returns and other information provided to the Division, the Division recalculated petitioners' tax liabilities under Article 9-A of the Tax Law, and the parties stipulated to the amount of the Article 9-A deficiencies as follows:

Period Ending	9/30/85	9/30/86
Amherst	$ 96,626.00	$133,985.00
Comax	None	$197,536.00
Ken-Ton	$125,040.00	$226,280.00

Petitioners presented testimony at hearing intended to support their claim that unlike the petitioner in Capital Cablevision they operated transmission companies properly taxable under Article 9. They also presented evidence and testimony to show that they would be unfairly prejudiced by the retroactive application of the decision in Capital Cablevision. The direct testimony of David Justice, petitioners' comptroller during the years in issue, described petitioners' calculation of the gross receipts tax under Article 9 in order to support their contention that petitioners would have filed combined reports and treated expenses differently if they were filing as Article 9-A taxpayers. The Division asked no questions of Mr. Justice regarding petitioners' calculation of the Article 9 tax in 1985 or 1986.

The Division presented no witness testimony of its own. It did offer in evidence an affidavit executed by Linda Martinez, a Division employee. Her affidavit states, in pertinent part:

"6. In 1987 I commenced a franchise tax desk audit of the Article 9 Franchise Tax reports filed by Amherst Cablevision Inc. (Amherst), Comax Telecom Corporation (Comax) and Ken-Ton Cablevision Inc. for the year 1985.

* * *

"8. Based on the information available, I recomputed tax due from these companies under Article 9. On August 29, 1988 Article 9 deficiency notices were issued to Amherst, Comax and Ken-Ton.

"9. After Amherst, Comax and Ken-Ton timely petitioned the Article 9 deficiency notices, the Tax Appeals Tribunal issued its decision in Matter of Capitol [sic] Cablevision Systems, Inc.

"10. From June, 1988 forward the Audit Division's policy was to follow the legal precedent established by the Tax Tribunal in Capitol [sic] Cablevision and, as a consequence, the Audit Division classified all cable television companies as Article 9-A taxpayers for all open tax years.

"11. Based on the Audit Division's policy described in paragraph 10, I computed franchise tax due from Amherst Comax and Ken-Ton under Article 9-A of the Tax Law using information taken from the companies [sic] franchise tax reports."

Attached to the affidavit were three letters sent by Ms. Martinez to Ken-Ton, Comax and Amherst, respectively, in the course of her Article 9 audit. In those letters she requested additional information to supplement franchise tax reports filed by Amherst and Ken-Ton for 1985 and by Comax for 1986. Her letter to Comax states, as relevant here:

"Gain on the sale of investments of all types, (governmental and non-governmental) and gain on the sale of properties located or from sources in this state are taxable. To compute the gain on the sale of property, the cost, not book value, less any expenses incurred in making the sale, is used.

"Using the above paragraph as a guideline, please compute the tax due on the sale of intangibles in the amount of $46,207,611.00."

No other evidence was offered by the Division to explain its calculation of tax deficiencies under Article 9.

On August 31, 1993, petitioners filed a brief in which their principal arguments were (1) that petitioners were principally engaged in a transmission business and were subject to tax under Article 9 of the Tax Law, (2) that the retroactive application of the decision in Capital Cablevision is unlawful, (3) that the Division was equitably estopped from retroactively applying the decision in Capital Cablevision.

On September 23, 1993, the Tax Appeals Tribunal issued a decision (Matter of Newchannels Corp., supra) which generally supported petitioners' contentions. The administrative law judge then granted the Division's request for an extension of time in which to

file a responsive brief.

In lieu of a brief, the Division sent a letter to the Administrative Law Judge, dated December 9, 1993, where it stated its position as follows:

> "On September 23, 1993, the Tax Appeals Tribunal ruled in Newchannels Corporation, that Capitol [sic] Cablevision should be applied prospectively only. Accordingly, the Division no longer asserts that the petitioners must be taxed under Article 9-A for the tax years 1985 and 1986, years prior to the 1988 decision of Capitol [sic] Cablevision.
>
> "The Division agrees with petitioners' contention that they should be taxed under Article 9 for the tax years in issue. However, the question remains whether petitioners owe tax under Article 9. In summary, the fact that an additional/supplemental deficiency asserted can not [sic] be sustained does not invalidate the tax originally asserted due based on a premise petitioners contend was correct. Because the parties have not focused on the computation of the Article 9 deficiencies, the record should be reopened to allow the parties to submit proof as to this issue."

Because new issues were raised by the Division's letter, a new briefing schedule was established. Briefs were exchanged by the parties generally addressing the Division's assertion that petitioners' liability for Article 9 taxes is now the subject of this proceeding.

CONCLUSIONS OF LAW

A. The first issue to be decided in this proceeding is the one framed by the Division's attorney in her opening statement at hearing: whether the Division acted properly in asserting corporation franchise tax against petitioners under Article 9-A of the Tax Law. Based on the decision in Matter of Newchannels Corp. (supra), the parties now agree that petitioners were not subject to the tax imposed under Article 9-A in the assessment years. Consequently, any assessments issued to petitioners under the authority of Article 9-A are cancelled.[3]

B. The next issue to be addressed is whether, in this proceeding, the Division may assert taxes due against petitioners under Article 9 of the Tax Law. The Division argues that the

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[3]Tax Law § 1089(d)(1) provides that where a petition has been filed the Tax Appeals Tribunal "shall have power to determine a greater deficiency than asserted in the notice of deficiency and to determine if there should be assessed any addition to tax" if a claim for additional tax is made at or before the hearing. Whether this provision actually provided the Tax Appeals Tribunal with the authority to determine a tax deficiency against petitioners under Article 9-A after the Article 9 assessments were issued and petitioned need not be considered here since both parties agree that no tax is owed under Article 9-A.

notices of deficiency issued under the authority of Article 9 of the Tax Law were never cancelled, but rather, were revised to reflect additional deficiencies under Article 9-A. Although the Division concedes that the Article 9-A assessments should be cancelled, it claims that the Article 9 assessments remain standing. Before assessing the Division's argument, it will be helpful to recap some of the events which occurred after the Article 9 notices of deficiency were issued.

Following the issuance of those notices, the Tax Appeals Tribunal issued its decision in Matter of Capital Cablevision Systems (supra). The Division then made the decision to assess tax against petitioners under Article 9-A of the Tax Law. The Article 9 notices of deficiency issued to Amherst and Ken-Ton for 1986 were initially cancelled and notices of deficiency were issued under Article 9-A. The cancellation notices were later withdrawn, or deemed to be a nullity, by the letters of December 29, 1989. In those letters, the Division asserted Article 9-A liabilities against petitioners as additional deficiencies under the original notices of deficiency. Similar letters were sent to Amherst and Ken-Ton for 1985. From that point until the completion of the administrative hearing on May 26, 1993, the Division repeatedly stated that it had changed its theory of liability from Article 9 to Article 9-A.

In response to Judge Alston's statement: "You take the position that the Notice is still good, but you're asserting liability under the other article, correct?" The Division's attorney responded: "That's correct." The Division then filed an amended answer for the 1986 tax year where it stated that cable television companies are taxable under Article 9-A of the Tax Law. It made no mention of Article 9 of the Tax Law. In her opening statement at the continued hearing, Ms. Dwyer stated that the issue before the Administrative Law Judge was whether the Division had properly asserted tax against petitioners under Article 9-A of the Tax Law. Finally, the Division executed a stipulation which states: "[t]he Department does not assert any Tax Law Article 9 deficiency against Amherst, Comax or Ken-Ton for calendar years 1985 or 1986."

The Division now argues that none of these intervening events have any effect on the

viability of the Article 9 assessments. I disagree and conclude that the Division is bound by its stipulation, its amended answer and the statements of its representative at hearing. The Division's arguments in favor of restoring the Article 9 assessments are meritless.

The Division argues that petitioners' reply to the amended answer shows that petitioners recognized "that the original Article 9 assessments had not merely vanished" (Division's Letter, May 5, 1994). In its reply pleading, petitioners asserted that the Division had the burden of proof with respect to the tax asserted under Article 9-A "over amounts previously assessed against and protested by Petitioners under Article 9." Also, in their claim for relief, petitioners requested that both the Article 9 and Article 9-A deficiencies be cancelled. I agree with the Division that the reply pleading shows that petitioners understood, at that point in the proceeding, that the Division might still assert taxes under Article 9. Consequently, petitioners pleaded, in the alternative, that both the Article 9 and Article 9-A assessments should be cancelled. The reply was served in June 1991. In November 1991, the Division stipulated that "the Department does not assert any Tax Law Article 9 deficiency against Amherst, Comax or Ken-Ton for calendar years 1985 or 1986." The stipulation, coming later in time than the pleadings, takes precedence over those pleadings (see, Matter of Nelson, Tax Appeals Tribunal, September 12, 1991). In short, as of the date of the stipulation, the Division represented that it was no longer seeking to pursue its Article 9 claims.

The stipulation is consistent with the statements made by the Division's representative at hearing. The Division attempts to minimize the impact of Ms. Dwyer's hearing comments, stating in its letter of May 5, 1994:

> "[The Division's attorney] did say with respect to the Notice of Deficiency under Article 9 'They were, in essence, cancelled and new deficiencies issue[d] under Article 9-A'[.]However, the excess [sic] of this statement was corrected in the very next statement by ALJ Corigliano 'Meaning the letter issued in December 1989'[.] As stated above, the December 29, 1989 letter explained that **cancellation** of prior Article 9 Notices of Deficiencies were nullified and additional deficiencies under Article 9-A were asserted." (Division's letter, May 5, 1996, p. 6; emphasis in original.)

The fact that the December 29 letters purported to nullify the previous cancellations of the 1986 Article 9 deficiencies cannot nullify the position taken by the Division at hearing --

that the Article 9 tax liabilities "were, in essence, cancelled."

Finally, the Division contends that the stipulation it executed should not be accepted. The Division notes that a stipulation may be rejected where it exceeds its authority, for example, by stipulating to the admissibility of evidence. The Division does not explain why it believes that the parties lacked the authority to narrow the legal issues by stipulating that the Division "does not assert any Tax Law Article 9 deficiency against Amherst, Comax or Ken-Ton".[4] Citing to Loftin and Woodward, Inc. v. United States (577 F2d 1206), the Division also states that where it would be manifestly unjust to accept a stipulation or where there is substantial evidence contrary to the stipulation the stipulation may be disregarded. Although an Administrative Law Judge may permit a party to qualify, change or contradict a stipulation where justice requires it (20 NYCRR 3000.7[e]), I find groundless the Division's claim that "justice requires" the Division of Tax Appeals to now restore the Article 9 assessments.

Contrary to the Division's contentions, an examination of the hearing record does not show "that sufficient documents were introduced into the record to set up the Divisions [sic] case under Article 9 so that it fell to the petitioners to meet their burden of proof" (Division's letter, May 5, 1994, p. 5). The documents the Division refers to are: (1) the original notices of deficiency; (2) the letters of September 16, 1988 and December 29, 1989, asserting additional deficiencies under Article 9-A; (3) the affidavit of Linda Martinez; and (4) the letters attached to her affidavit. The first two items were introduced to establish that the Division of Tax Appeals had jurisdiction to consider deficiencies under Article 9-A.[5] Ms. Martinez's affidavit

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[4]By citing to Matter of Willett v. Chu (124 AD2d 375, 507 NYS2d 318), the Division suggests, rather than explicitly stating, that its representative acted outside the scope of her authority. In Willett, the Division's attorney conceded at hearing that the petitioner's business activities constituted the practice of a profession and thus were exempt. The State Tax Commission found that those activities did not fall within the professional exemption. The court held that the attorney's misstatement was not binding on the State Tax Commission. The same facts do not exist here, where the stipulation was in writing, rather than verbal, and the Division has not claimed that its attorney acted without authority.

[5]After the notices of deficiency were issued under Article 9 of the Tax Law, the Division took the position that it could assert Article 9-A taxes by piggybacking those taxes on the existing

and the letters attached to it did not place the Article 9 deficiencies in issue. In fact, it would not have been possible for the Division to "set up . . . [its] case under Article 9", without first moving for an order allowing it to withdraw its stipulation.

The heart of the Division's position may be found in this statement:

> "The Division maintains that its retroactive application of Capitol [sic] was the only reasonable way to implement that decision and that it could not have reasonably expected the Tribunal Decision in Newchannels. If the Capitol [sic] Cablevision decision provided any indication that the Tax Appeals Tribunal would not follow the general rule on retroactivity cited above, but instead would make an unusual and liberal application of Chevron the Division would have continued to treat all similarly situated cable television companies as Article 9 taxpayers. The Division would have pursued only the Article 9 deficiencies in this case and the procedural confusion, which the petitioners hope to profit from, would not have occurred. The Division of Tax Appeals should not now absolve the petitioners of their bold substantial understatements of gross earnings under Article 9 by giving legitimacy to their arguments of alternative pleading." (Division's Letter, May 5, 1994, p. 10.)

The Division itself gave legitimacy to petitioners' arguments of alternative pleading in its letter of December 9, 1993, where it stated:

> "The Article 9 and Article 9-A taxes are mutually exclusive. Tax Law § 209(4). Therefore, the fact that the Division may have misclassified a taxpayer does not preclude the assertion of tax due under the correct tax article, particularly when that tax has been determined due on audit. This case is analogous to a situation where a taxpayer files a nonresident return and the Division asserts a deficiency based on the theory that the taxpayer is a resident but also believes that New York source income is incorrectly computed. The Division may pursue tax under alternative theories." (Letter of the Division, December 9, 1993, p. 4; emphasis added.)

In its pleadings, petitioners consistently alleged that the Tax Tribunal's holding in Matter of Capital Cablevision Systems should not be given retroactive effect. In her opening statement at the continued hearing, Ms. Dwyer alluded to petitioners' position, demonstrating that the Division clearly understood that the retroactive application of the Capital Cablevision decision

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Article 9 notices of deficiency. However, as Ms. Dwyer's numerous statements made clear, this was merely a procedural mechanism. The December 29, 1989 letters to petitioners did not assert tax under Article 9 and additional tax under Article 9-A. The letters revised the original assessments by calculating the franchise tax due under Article 9-A of the Tax Law. The Division's repeated statement that the December letters asserted "additional deficiencies" is misleading.

was one of the issues raised in this proceeding. Since it was an issue (and in reality it was the major issue of this case until Newchannels was issued), the Division must have known that petitioners' position on the issue of retroactivity might prevail. The Division had every opportunity to assert a claim under Article 9 in the alternative in order to preserve that claim if it failed to prevail on the issue of retroactivity. It did not do so; rather, it agreed by written stipulation to drop its claim for Article 9 taxes. I fail to see the injustice in binding the Division to its stipulation.

C. The petitions of Amherst Cablevision, Inc., Ken-Ton Cablevision, Inc. and Comax Telecom Corporation are granted; the notices of deficiency issued to Amherst Cablevision, Inc. and Ken-Ton Cablevision, dated October 30, 1987 and January 4, 1989 are cancelled; and the notices of deficiency issued to Amherst Cablevision, Inc., Ken-Ton Cablevision, Inc. and Comax Telecom Corporation, dated August 29, 1988, are cancelled; and the notices of deficiency issued to Amherst Cablevision, Inc. and Ken-Ton Cablevision, Inc., dated September 27, 1989, are cancelled.

DATED: Troy, New York
November 10, 1994

/s/ Jean Corigliano
ADMINISTRATIVE LAW JUDGE